Service Date: April 29, 1988

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

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IN THE MATTER of the Application of GREAT FALLS GAS COMPANY for Authority to Increase Rates for Natural Gas Service and to Restructure Tariffs.	)	UTILITY DIVISION DOCKET NO. 87.7.37 ORDER NO. 5313a

I. BACKGROUND

On November 24, 1986, the Montana Public Service Commission (PSC or Commission) initiated Docket No. 86.11.62, with Order 5236, which was an Order to Show Cause. That order requested utilities to demonstrate that existing rates for public utilities remained just and reasonable following the Tax Reform Act (TRA) of 1986. Great Falls Gas was assigned Docket No. 86.11.62 (5). All respondents were ordered to provide the information required by the Commission's minimum filing requirements on or before February 1, 1987.

On December 4, 1986, the PSC received a Motion for Reconsideration from Great Falls Gas Company (GFG, Company or Applicant) requesting that it be allowed until June 1, 1987, to make its compliance filing under Order No. 5236. On December 15, 1986, the Commission granted the Applicant's Motion for Reconsideration.

On May 26, 1987, the Commission received a request for an extension of time from GFG requesting that it be allowed until July 1, 1987, to make its compliance filing. On May 26, 1987, the Commission denied the Applicant's request.

On June 2, 1987, GFG made its compliance filing pursuant to Order No. 5236 (compliance filing). The cost of service in the compliance filing showed a need for additional revenues of $204,624. Included in the compliance filing was a stipulation between GFG and the Montana Consumer Counsel (MCC) on the cost of capital. The date of this stipulation was June 1, 1987. The company used a test year ending March 31, 1987, adjusted for known and measurable changes.

In a letter to the PSC staff dated July 2, 1987, John Allen indicated that two changes needed to be made to the compliance filing cost of service. First, the MCC and PSC taxes increased by $7,643. Secondly, an error was made in the calculation of revenues from the Commercial Market Retention rate in the amount of $9,547. Those two changes in the cost of service resulted in a total revenue increase of $221,548.

On July 27, 1988, the Commission issued Interim Order No. 5281 in Docket No. 86.11.62 (5). That order reduced rates on an interim basis by $116,677 annually.

On July 29, 1988, GFG filed an application which requested an increase in rates of $221,548. This application was assigned Docket No. 87.7.37. Included with the filing was a request to consolidate Docket No. 86.8.38 (Malmstrom load loss) and Docket No. 86.11.62 (5) (TRA) into Docket No. 87.7.37.

On September 23, 1987, the Commission issued a Notice Of Commission Action which stated that the PSC voted to consolidate the following pending dockets into Docket No. 87.7.37 for further consideration and final disposition: 86.11.62 (5) (TRA); 86.8.38 (Malmstrom load loss); and 86.12.75 (Commercial Market Retention Tariff).

On December 14, 1987, the Commission issued Interim Order No. 5313, which increased the surcharge for the No-Interest Loan Program from $.0111 per Mcf to $.0548 per Mcf.

On January 21, 1988, the PSC received an application from GFG for approval to utilize random sampling in their meter change out program. On February 1, 1988, the PSC voted to consolidate this issue into Docket No. 87.7.37.

On February 25, 1988, the Commission issued a Notice of Public Hearing in Docket No. 87.7.37.

On March 4, 1988, the Commission received a stipulation between GFG and MCC. This stipulation purported to resolve all issues in this proceeding, which were contested as between GFG and MCC.

On March 22, 1988, pursuant to the Notice of Public Hearing, a hearing was held in the Bonanza Room of the Ponderosa Inn, 220 Central Avenue, Great Falls, Montana. At the hearing, the Company requested that the Commission take administrative notice of the prefiled testimony and exhibits in this proceeding. There were no objections to this request. Accordingly, and to offer a complete record, the Commission takes administrative notice of all prefiled testimony and exhibits in this procedure, as well as all discovery which was conducted in connection with this proceeding.

MCC has participated in this Docket on behalf of gas utility consumers since the inception of these proceedings.

II. COST OF CAPITAL AND REVENUE REQUIREMENTS

STIPULATIONS

There are two stipulations which have been presented to the Commission for consideration. The first stipulation was filed on June 2, 1987. It contained a 50/50 debt equity ratio, a cost of debt of 9.16 percent and a cost of equity of 12.25 percent. The overall cost of capital in the stipulation was 10.71 percent. Although concerned about the equity ratio in the capital structure, the Commission finds that the rate of return stipulation to be reasonable and hereby approves the stipulation on a final basis. The equity return of 12.25 percent may be used to set the return on equity in the Company's next interim order.

The second stipulation is much larger in scope. On March 4, 1988, the Commission received a stipulation between GFG and MCC which increased rates by $116,677. This returns rates to levels existing prior to the interim order in Docket No. 86.11.62 (5). GFG will receive none of the increase it requested in this Docket. As with all stipulations, there are positive and negative aspects to the proposal. From a revenue requirement perspective, the Commission approves the stipulation. For a number of years, both the Commission and GFG have struggled with the appropriate volumes to assign to the Malmstrom load. The stipulation sets volumes for Malmstrom at 443,267 Mcf and eliminates both the overcollection from Docket No. 86.8.38, and the balancing account associated with the Malmstrom load. Similarly, the stipulation also eliminates the

SPI balancing account and sets volumes for the Montana Refining Company at 201,268 Mcf.

TAX REFORM ACT

GFG complied with the Commission's Order No. 5236c in the Tax Reform Docket No. 86.11.62 (5). Rates are now based on the findings in that order. Accordingly, this Order closes Docket No. 86.11.62 (5).

METER CHANGE OUT PROGRAM

GFG requested that the rules for meter testing be changed to allow random sampling of meters. The Company noted that a similar program has been approved for MDU on July 2, 1973. The Commission approves the change in rule 15 of its service regulations for GFG with one condition. All meter groups must be subject to random sampling.

GAS RESEARCH INSTITUTE

In this Docket, the Company proposed to increase the surcharge for the Gas Research Institute from $.0125 per Mcf to $.0152 per Mcf. After reviewing Exhibit #___(LDG-1), the Commission finds that continued support of this research is warranted and approves the new surcharge of $.0152 per Mcf.

NO_INTEREST LOAN PROGRAM

As noted in Finding No. 9 above, the Commission has approved a surcharge of $.0548 per Mcf in Interim Order No. 5313. The Commission approves this surcharge on a final basis, and notes that the cost effectiveness of the no-interest loan program will be examined in future Dockets.

III. COST OF SERVICE

BACKGROUND

The last docket in which cost of service was at issue for the Company was Docket No. 6701. An order was issued (No. 4602a) in May of 1980 in this Docket. That order denied GFG's proposed Seaboard costing approach in favor of a volumetric cost allocation approach. The Commission's reasoning focused on the relative scarcity of gas, as reflected in the marginal cost incurred by GFG, although GFG held capacity was relatively more scarce.

The Commission's rate design determinations in Docket No. 6701, except as noted below, remained largely intact until the present time. Based on "inverse elasticity principles", and costs and revenue requirements at the time, the Commission denied tariffing of service charges. Also, based on marginal cost considerations the Commission denied declining-block prices.

Since 1980, and until recently, cost of service and rate design for GFG has not generally been contested. Increased fuel price competition, however, has impacted certain of the Company's loads. In Docket No. 85.7.26 (Order No. 5153a), the Commission approved GFG's Special Propane Based Interruptible Industrial Gas (SPI) tariff. What this tariff really accomplished was retention of the Montana Refinery load in the face of falling competitive fuel prices.

Since GFG filed the SPI tariff, the Company also submitted a Commercial Market Retention (CMR) tariff (Docket No. 86.12.75), which is an issue in the present docket. The Commission granted interim approval of the CMR tariff in Order No. 5253.

Great Falls Gas. GFG employed the services of Mr. Richard Rudden to perform Cost of Service (COS) studies. Mr. Rudden prepared both marginal and fully allocated cost studies. Mr. Rudden's studies argue for shifting revenue to the residential class.

Montana Consumer Counsel. MCC employed Mr. Jim Drzemiecki (hereafter MCC) to perform an embedded class cost of service study and develop rate design proposals. MCC also critiqued Mr. Rudden's studies. MCC's COS results also argued for shifting revenue requirements to the residential class.

COMMISSION'S DECISION REGARDING THE CLASS COST OF SERVICE STIPULATION

GFG and MCC stipulated to cost of service issues in this Docket. The stipulation allocates the total increase in revenue requirement of $116,677 entirely to the Residential Class. The stipulation also set out annual MCF volumes for each class.

As to the cost of service, the Commission approves the stipulation, but with certain comments. First, the Commission notes that it has supported using marginal cost analyses to, in part, determine class revenue requirements. In this regard, the MCC seems to raise valid concerns with GFG's marginal cost study. In particular, GFG's use of annual billing determinants to allocate capacity costs appears to be illogical. However, the Commission was pleased with GFG's move towards marginal cost analyses.

Second, it is not clear that GFG's method of computing distribution capacity costs results in efficient resource allocation. A flawed line extension policy can result in costs clearly associated with unique cost causers being subsidized by the general body of ratepayers.

The Commission was surprised to see the MCC's embedded COS study in this Docket, rather than a marginal cost study such as the MCC performed for the MPC gas Docket No. 87.8.38. The change in perspective from an embedded study to a marginal cost study may not materially change the inter-class revenue requirements stipulated to by the Company and the MCC. The Commission assumes MCC's philosophy that rates of return from proper marginal cost studies only should be used to allocate revenue requirements to classes, is unchanged (e.g., MDU gas Docket No. 85.7.30, Order No. 5160a, Finding No. 131).

IV. RATE DESIGN

Background

Efficient resource allocation concerns have largely guided the Commission's past pricing decisions, including those involving GFG. For example, in Docket No. 6701, the Commission relied on "inverse elasticity" arguments to not tariff service charges.

At present GFG has only three tariffs with prices as summarized in Table 2 below.

TABLE 2

Current Prices
Great Falls Gas Company

Class	Price ($/Mcf) Base Rate	Effective Rate
Firm Natural Gas	4.0597	4.0833
Commercial Market Retention:		
< 50,000/Yr		4.0833
> 50,000/Yr		3.3417 (est)
SPI:		
less than 200,000/yr		3.9379
next 50,000/yr		3.8311
more than 250,000/yr		3.7243

Source: The Firm rate is from the tariff. The Commercial Rates are computed by adding the ZIP and GRI surcharges after applying the lost and unaccounted for (1.0127) plus 10 percent (1.10) multiplier (see PSC 304i). The SPI tariff also includes a ZIP ($.0548) and a GRI adder ($.0125). There is also a trigger mechanism on the SPI tariff in the case Propane prices exceed $.41 delivered in Great Falls and the price change exceeds 1.5 percent.

GFG has proposed to more than double the number of tariffs on which it provides gas service. This proliferation of tariffs and varying rate designs reflects, in part, increased competitive fuel opportunities available to certain of the Company's customers. The following reviews, in turn, the Commission's understanding of the Stipulation on rate design followed by the Commission's decision.

RATE DESIGN STIPULATION

GFG and MCC stipulated to certain rate design issues. The relevant part of the Stipulation reads:

> The parties agree that the applicant's proposed customer classes, service charges, and rate blocks are appropriate except that in the case of Malmstrom no declining block is necessary due to the new stipulated volume level. (see Paragraph No. 10)

This part of the stipulation indicates that the MCC concurs with every proposed customer class and price structure in GFG's initial testimony except for the Malmstrom declining-block price structure. Exhibit A, from the hearing, in turn, included tariffs for all such customer classes, and also a "Special Service Tariff". The following reviews the tariffs stipulated to by GFG and the MCC.

Residential Service. GFG's proposed tariff features a customer charge of $3.00/Month and a nonlinear declining block commodity price structure. The initial and tail block prices would equal $3.77 and 3.7128 respectively. These prices are unchanged on Exhibit A (Exhibit A was a Company handout at the hearing that summarized the Company's tariff proposals). The commodity prices would be adjusted upwards to recover ZIP and GRI charges.

General Service. GFG's proposal makes this tariff available to certain commercial, industrial, Housing Authority, governmental agency customers and apartments with more than two units. Loads on this tariff are not interruptible. The customer charge would equal $7.00/month. A four-step declining block commodity tariff is proposed as noted below. These are the same prices in Ms. Rice's rebuttal testimony and Exhibit A:

First 10 Mcf	$3.7700
Next 90 Mcf	3.7128
Next 900 Mcf	3.6880
All excess	3.6450

Large Dual Fuel. GFG proposed renaming the existing Commercial Market Retention (CMR) tariff the Large Duel Fuel (LDF) tariff. This tariff would be available for customers using in excess of 20,000 Mcf per year. The tariff has the following features: 1) a customer charge of $400 per month; 2) a nonlinear five (5) step declining block commodity price structure (GFG Data Response to PSC 304-ii). The first four blocks derive from the GS tariff. All volumes exceeding 50,000 Mcf would be sold at "...the cost of gas...plus 10%." The LDF is not an interruptible tariff.

The purpose of this tariff is to check load losses due to customers switching to oil.

<u>Special Propane-Based Interruptible Gas.</u> GFG has proposed to make substantial changes to the SPI tariff. GFG's initial proposal and its summary in Exhibit A appear identical and include the following features: To qualify for this tariff a customer's volumes per year must exceed 100,000 Mcf; The load is interruptible and/or curtailable but with at least six hours notice (GFG Data Response to PSC-100-iii); The only price ele ment is a commodity price based upon the cost of gas plus 10 percent, and this price is for all consumption. GFG proposes a lost and unaccounted for adjustment of .5 percent and the above ZIP and GRI adjustments. These adjustments are added after the 1.1055 percent markup (GFG Data Response to PSC 305-iv). The Company believes that parity will be maintained between the SPI price and the delivered price of propane (PSC-305-iii-a).

<u>Malmstrom Air Force Base.</u> The MAFB tariff is available to Malmstrom or "...any other customer who now or in the future demonstrates the same service characteristics." GFG revised this tariff in Exhibit A to reflect the Stipulation. The MAFB tariff features two parts, a service charge of $12,500/Month and a

commodity price. The stipulated tariff includes a single commodity price of $3.49/Mcf adjusted for the GRI and ZIP adders. No loss adjustment is made. The MAFB load is neither interruptible or curtailable.

Natural Gas Incentive Sales Rate. The NGI tariff is a new offering and quite complex relative to any other GFG tariff. First, it is applicable to all General Service or "Special Contract" customers who utilize gas for either cogeneration, air conditioning or a vehicle fuel. Either new or existing customers can qualify. New customers must consume at least 8,000 Mcf annually or agree to face a take or pay condition. An existing customer must only increase its demand. A minimum 3-year con tract is required for any customer. That is, the life of this tariff exceeds 3 years.

The version of the NGI tariff in Exhibit A, which was presented at hearing includes only a nonlinear two-step declining block commodity price structure. However, GFG's initial tariff included service charges that depended on whether the customer is new ($12.50/mo) or existing ($7.00/mo), and a complex commodity price structure. The MCC, in hearing, did not contest the changes to this tariff as reflected in Exhibit A. Accordingly, the

Commission concludes that these changes are part of the stipulation.

Transportation Service. The TS tariff is only available to the Company's General Service customers, and only then if they have executed a separate TS contract with GFG. That is "Special Contract" customers (ie, Malmstrom, SPI and LDF) may not receive transportation service (Data Response No. PSC 308-iv).

The TS tariff features volumetric prices and a minimum bill provision. The TS commodity price structure is nonlinear and also varies by the quality of service. Three types of service are available to any qualifying customer: 1) all firm, 2) firm and interruptible and 3) all interruptible. The "all Firm" TS customer faces a nonlinear 3-step declining block price structure. The firm price blocks are: 1) first 100 Mcf at $.88, 2) the next 900 Mcf at $.85 and 3) all excess at $.81.

The transportation rate for firm service was computed as roughly equal to the margin in each of the blocks of the GS tariff (the proposed GS rate block minus the base cost of gas of $2.835).

The "firm and interruptible" option features the same nonlinear price structure for the first 1000 Mcf per month. The interruptible price is $.40/Mcf for all volumes over 1000 Mcf/Mo. The "all interruptible" price is $.40/Mcf. The basis for the interruptible rate is simple division by two of the firm price for volumes over 1000 Mcf.

Special Service Tariffs. GFG proposed four new special service tariffs, a reconnection charge ($15), a Nonsufficient Funds (NSF) Check Charge ($10), a damaged meters charge ($135) and an Access Refusal charge ($250).

COMMISSION DECISION REGARDING THE RATE DESIGN STIPULATION

This section is organized as follows: First, the stipulation is discussed; Second, the Commission reviews tariff issues on a "core/noncore" customer class basis.

The Commission finds that, as a result of the Stipulation, MCC and GFG agree to each of the seven customer class tariffs included in GFG's initial testimony, as finally reflected in Exhibit A. The Commission does not believe the "Special Service Tariffs" are included in the Stipulation. MCC did not contest this aspect of the Company's filing, as reflected by the prefiled testimony of Mr. Drzemiecki. Obviously, only "contested" issues may later be resolved by a stipulation. Further, the "Special

Service Tariffs" are not a customer class. Accordingly Commission finds that the "Special Services Tariffs" are outside of the context of the Stipulation.

The Commission finds no reason to reject the rate design aspects of the Stipulation. All proposed service charges, and rate structures are approved as appear in Exhibit A. However, the Commission is uncomfortable with certain aspects of the Stipulation, as discussed below.

Core Customer Tariffs. The Commission defines core customer classes generally to include Residential, General Service (small business), and Industrial (large business). In this Docket, GFG's proposed Residential and General Service tariffs are examples of core customer loads. The MAFB tariff appears to be another example.

While the Commission has concern with the impacts of the stipulated prices for these classes, the Commission finds appropriate the pricing proposals in this Docket. Pricing decisions should reflect the dynamics of changing costs over time. The "inverse elasticity principles" argument used by the Commission in 1980 (Docket No. 6701) to oppose service charges, if used today with today's costs and revenue requirements, would argue for declining block prices and/or service charges. Again, however, the process is a dynamic one. When costs significantly change, price structures will have to be revisited. Hopefully, the Company will not let eight years pass before the next thorough costing/pricing review.

Noncore Customer Tariffs. In the present filing GFG has proposed changes to and/or modified a number of tariffs that appear to be for noncore loads. These tariffs appears to include the SPI, LDF, and NGI. In addition, the transportation tariff, while limited to General Service loads, may, in part, serve what evolves as noncore loads.

While the Stipulation sanctions these noncore tariffs, it does not address an issue of concern to the Commission. The issue involves whether or not the Company's stockholders should share in the risk of pricing flexibility. The risks are twofold. First, with price flexibility, revenue generation from loads with alternative fuel burning capability will not be maximized. A second risk involves whether the prices charged cover relevant long run costs of service. Although the Commission is allowing GFG its requested price flexibility, it should be recognized that certain incentives may be appropriate. The following sets forth the Commission's concerns.

Incentive, Interruptible and Retention Objectives. The pricing of utility services has as a primary objective the setting of efficient prices. The Commission has a range of options to achieve this objective. A utility could have the same single average price for each and every customer. At the other end of the spectrum a separate deaveraged price for each and every customer could be tariffed. Both limits would result in pricing inefficiencies. The latter would create tremendous "transactions" costs, and the former would create tremendous "opportunity" costs. Until recently a few tariffs have sufficed.

There has been a flurry of tariff filings by regulated utilities with retention, incentive and/or interruptible (RII) load objectives. GFG is no exception. These three functions are not mutually exclusive, as tariff filings commonly feature two or more of these objectives. The result is numerous additional layers of cost separability and pricing complexity.

One can question why there has been a flurry of RII filings by energy utilities. One logical explanation flows as follows: Prior to the recent fall in nominal world oil prices (early 1986), utilities could aggregate customers into several customer classes. When oil prices fell, unregulated petroleum prices naturally decreased. In turn, unregulated competitive fuel prices (e.g., propane) were reduced to remain competitive. In order for regulated utilities to retain load and remain competitive, their prices also must fall. In any case, the recovery of fixed and common cost becomes an issue of concern.

Recent RII tariff filings by utilities in Montana can themselves feature averaged prices or price flexibility. Herein rests one of the Commission's concerns with risk sharing. MPC, for example, has filed gas tariffs (Industrial Market Retention and Natural Gas Incentive, IMR and NGI respectively), that feature price flexibility within ceiling and floor bounds. On an interim basis, the Commission has required MPC to absorb 10 percent of the difference between the otherwise applicable rate and the price at which gas is sold on the IMR-86 tariff. This provision was included, in part, as an incentive mechanism, so that MPC would negotiate in the best interests of other ratepayers.

GFG, on the other hand, has sought to achieve the same objectives, but not by filing a single tariff with price flexibility. Rather, GFG has proposed separate tariffs for customers with similar alternative fuel opportunities. That is, what MPC has accomplished with generic retention and incentive tariffs, GFG proposes to accomplish with customer specific (SPI, LDF, NGI and possibly MAFB) tariffs. The issue of risk sharing, however, arises with either MPC's or GFG's approach. The following will discuss each of the noncore tariffs from the perspective of the appropriateness of risk sharing.

SPI. The SPI is available to all qualifying loads. However, only one load, the Montana Refinery, apparently qualifies given the 100,000 Mcf per year minimum consumption requirement. The SPI price floor is the cost of gas plus 10 percent, but that price maintains parity with the delivered cost of propane (GFG Data Response No. 305iiia to PSC). Further, there is no sunset for this tariff. Finally, and importantly, the SPI load is interruptible.

The Commission believes that, at this time, it is probably not appropriate for shareholders to share in the risk of this tariff. From a cost perspective the only qualifying load, the Montana Refinery (MR), is a large load, very price elastic and has unique cost characteristics. That is, MR's load exceeds 200,000 Mcf/year, propane is a cost effective fuel substitute, and MR's interconnect involves only 175 feet of pipeline to City Gate #1

(Data Response No. PSC-97). Hence, transactions costs, relative to revenues, are minimal.

Although the Commission will not require GFG's shareholders to share in the risks of the SPI tariff in this Docket, the Commission believes that it may be appropriate for MR to ultimately bear the full cost of any replacement or new capital investments associated with its gas loads.

This belief, in turn, stems from three areas of concern the Commission has with GFG's marginal cost study. Each concern relates to an apparent underestimate of the SPI class' relevant long run costs in the Company's class cost of service study. First, GFG has stated that the average remaining life of the MR interconnect is about 10 years (Data Response No. PSC 42i). GFG has not performed and would not provide an estimate of the replacement cost of the interconnect (<u>ibid</u>., part 42ii). The Commission believes that the same costs are relevant to, and are absent in, the Company's marginal cost study (see Exh. No. RJR-4).

Second, and contrary to the Company's statement in Data Response No. PSC 314a, Mr. Rudden's marginal cost study, as summarized on Exhibit No. RJR-4, <u>does not include</u> "...the value of meters and regulators for all customer classes." The marginal customer cost entries are zero for the SPI class. Moreover, in Data Response No. PSC-315, GFG concedes the relevance of the same costs: "Sunk costs pertaining to meters and regulators have actual positive opportunity, since they can be moved to another location and used with another customer."

While the above summarizes two cost related concerns involving risk sharing, the Commission has a third concern that relates to the unique interruptible nature of the SPI tariff. The concern ties together the need for interruptible loads and interruptible price incentives. It is worth noting that GFG has performed no system analysis of either the optimal amount of interruptible load, or the optimal price incentive required for interruptible load. An explanation of each follows.

Certain facts are pertinent to this third concern. First, GFG has not had to interrupt any loads since 1980, and possibly even earlier than this date (Data Response No. PSC-84ii). GFG has experienced an approximate 33 percent reduction in its 24 hour system peak demand from 1980 to 1987, with 1983's peak of 42,908 Mcf being the highest 24 hour peak since 1980 (PSC Data Response No. PSC 79). GFG's high pressure system peak deliverability has been unchanged at 44,520 Mcf/day since at least 1980 (Data Response

No. PSC-107ii). GFG states "We believe MPC's peak load assignment to GFGC is higher than real life situation, after taking into account changes in our load since 1983..." (sic, Data Response No. PSC 320 iii). MPC's peak assignment to GFG equals 42,908 Mcf, a figure which GFG contends is too high because it does not reflect MAFB's reduced loads, conservation impacts, and potential interruptible load reductions ibid.

From the above discussion, it would be reasonable to question GFG's need for MR's total amount of interruptible load. GFG, however, is unclear on whether it has excess distribution capacity. On one hand, the Company stated "GFGC does not agree that it has excess capacity" (Data Response No. PSC-50i). Conversely, the Company also notes that "GFG does not have a scarcity of either natural gas or system capacity." (Data Response No. PSC 95ii).

The Company also seems confused on how interruptible loads impact peak demand allocations. The Company states "We do assign value to interruptible loads. They do not contribute to our peak day." (Data Response No. PSC-84iii, emphasis added) But then the Company notes "Interruptible loads have contributed to peak day demand, since gas continued to flow." (Data Response No. PSC-320iv, emphasis added). Finally, the Company states that interruptible customers are exempt from peak demand allocations because they are interruptible, not because they are actually interrupted.

To summarize, the above discussion raises concerns with the Commission. Because of the apparent flaws in GFG's marginal cost study the Commission believes that, at a minimum, it may be appropriate for the MR load to ultimately assume responsibility for all capital costs incurred by GFG to continue to provide gas service. Of course, if GFG served additional customer's on this tariff, or gas sold under this tariff replaced a fuel other than propane, the Commission's beliefs regarding on risk sharing may need to be reviewed.

MAFB. The Commission finds many, but not all, of the concerns raised with the SPI tariff to apply to the MAFB tariff. Hence, only a brief discussion follows. As with the Montana Refinery, the Commission believes that it may be appropriate for MAFB to ultimately be responsible for all capital costs associated with replacement and additional plant needed to serve MAFB gas loads (see Data Response PSC -94i through vii). However, and as noted with the SPI tariff, the Commission finds unnecessary, at present, any risk sharing by GFG shareholders.

LDF. By its definition, this tariff is clearly a "but for not" tariff. GFG states it has identified customers with the same size, cost and dual fuel capability (Data Response No. PSC 304iv). The proposed prices would not vary by customer, and the tariff currently serves more than one customer with the same alternative fuel burning opportunities (Data Response Nos. PSC 304iii and PSC 23).

The CMR/LDF filing is an example of a move towards price deaveraging. But for the LDF tariff, if prices were not deaveraged, GFG would lose these loads, as the otherwise applicable General Service rate is too high. On the other hand, GFG now argues that these customers were apparently subsidizing other customers and as a result, there is no need to have the prices on the LDF tariff maintain parity with the price of the alternative fuel. Further, the Company notes that it ". . . does not intend to permanently absorb the loss associated with this tariff." (Data Response No. 327 to the PSC)

One concern the Commission has involves the apparent inconsistency between this tariff and the SPI. With the SPI, GFG holds parity makes sense. With the LDF, GFG holds parity does not make sense. It is worth noting that it was alternative fuel price pressures and the associated revenue loss, not cross subsidy concerns, which prompted GFG tariff proposals to retain both loads. Since the Company does not propose parity pricing for LDF loads, the Commission has to wonder whether future relative price increases for alternative fuels will cause GFG to merge the LDF tariff back on the General Service tariff.

In spite of the errors in the Company's marginal cost study, deaveraging costs to form the LDF class appears cost jus tified. There does not appear to be any need, at present, for shareholders to absorb any foregone revenues associated with this tariff.

NGI. The third tariff is the Company's proposed NGI tariff. The version of the NGI tariff in Exhibit A features no service charge and a two-step nonlinear declining block price structure. The Commission believes that, for the following reasons, it may be appropriate for GFG's investors to absorb 10 percent of the difference between each sale on this tariff and the price on the General Service tariff. The Commission's reasons generally revolve around the accuracy of the Company's marginal cost study.

First, as GFG noted in its data responses, the Company has not experienced an interruption since at least 1980 (GFG Data

Response PSC 84ii). Why discount sales on the basis of interruptibility without any apparent need?

Second, there is no apparent sunset on this tariff, although contracts expire at the end of three years. Customers must sign a contract of at least three years in duration. There appears no evidence that the proposed prices will cover the long run costs of service. For example, MCC's point that GFG's allocation of marginal demand costs may be flawed is a relevant concern.

Third, there is no service charge on the tariff. The initial NGI tariff had two different service charges, but the version in Exhibit A has none. Ms. Rice's Rebuttal testimony does not explain the removal of the service charges, and in fact only states "Some of the tariff language is changed slightly" to explain the removal of service charges on the NGI tariff, a sorely inadequate explanation. Possibly the service charge on the otherwise applicable tariff picks up the associated customer costs on the NGI tariff. But there is, however, no supporting cost evidence.

Fourth, there is no evidence the proposed prices are efficient in the winter months. MPC, in part, allocates costs to customers based on their contribution to winter peak demands. It would not seem to make sense to encourage additional winter loads if the Company does not have excess capacity as it states in this Docket (Data Response No. PSC-50), combined with the fact that the remaining average life of the Company's distribution system is 15.5 years (Data Response No. PSC-4).

Finally, there is no evidence that the costs reflected in prices on the General Service tariff are not appropriate for additional loads.

As a result of the above, the Commission believes that GFG shareholders probably should absorb 10 percent of the difference between the price at which gas is sold on the NGI tariff and price at which the same gas would have been sold on the General Service tariff. However, the Commission chooses to not take action at this time. The Commission would note that MDU has included said risk sharing voluntarily in a recent filing (Docket No. 87.12.77). Pending Final Orders for MDU and MPC on this issue, the Commission chooses to not enforce risk sharing at this time. The issue, however, is not resolved.

<u>Transportation Rates.</u> The Commission has several concerns with GFG's and MCC's proposed transportation rates. These concerns involve the fixity of the prices, the unit of measurement, and the

issue of possible take or pay penalties. Each is discussed in turn.

It is not clear that GFG's proposed fixed average prices will be very robust over the long run. While there is a major difference between Montana Dakota Utilities (MDU) and GFG (MDU has the ability to accommodate third-party gas), we now know the problems that can arise with fixed prices. The practical difference between fixed and flexible prices involves the trade off in revenue generation/contribution. Fixed transportation prices may not maximize revenues.

The second point concerns potential cross subsidization. In a data response GFG concurs that under certain conditions, therm billing may be needed for transportation service instead of the proposed volumetric pricing (see GFG's Data Response to PSC 80).

A third concern involves take or pay (TOP) and is more contemplative in nature. To the extent MPC incurs TOP penalties as a result of GFG customers having gas transported, there may be need to quickly revise these tariffs. That is, if MPC for example is allowed to allocate any TOP, or similarly related costs, back to GFG that are associated with GFG's transporting gas, there may be need to recover the same costs in GFG's transportation prices. The

Commission will cross this bridge when the issue arises, if in fact it does.

Special Service Tariffs. The Commission approves all but the Reconnection Charge on GFG's Special Services Tariff. The Commission's reasons for denying the Reconnection Charge include the following: First, the utility is already permitted to assess a late-payment fee, as are other gas utilities; Second, and related, MPC does not have, and has not proposed a Reconnection Charge. Yet MPC has also proposed service charges; Finally the Commission is concerned that a Reconnection Charge only impacts those ratepayers that already have a difficult time paying their utility bills, and actually provides a disincentive for returning to the system after termination.

V. TARIFF IMPLEMENTATION

Recently, the Company was directed, on an interim basis, to reduce its rates to reflect the reduced costs of gas to the Montana Power Company. On reconsideration, the Commission allowed the Company to defer implementation of this reduction until the tariffs were filed to comply with the Commission's Final Order in this Docket. Docket No. 87.11.63, Order No. 5302b. Accordingly, the Commission consolidates the further consideration of Docket No.

87.11.63 into this Docket. As a result of this consolidation, rate implementation from this Docket is somewhat complex. Three separate aspects are discussed below, including: The need for a rebate; implementation of the stipulated tariffs, and; the phase-in of MPC's gas cost reduction.

MPC's rate reduction was given interim approval by the Commission for service on and after March 23, 1988. Because the reduction to GFG was postponed pending a final order in the present Docket, a rebate issue has emerged. In this regard, GFG is to make the following calculations and credit customer bills as follows: Using the stipulated volumes, GFG is to compute the overcollection that occurred between March 23 through May 2, the first day in the Company's May billing cycle; the overcollection must be accumulated by month and interest accrued based on a 12.25 percent cost of equity; the total rebate amount is to be used to reduce the Company's positive NIP account balance.

GFG is to implement the tariffs as approved in this Order for services on and after May 2, 1988. At the same time these tariffs are implemented, the Company is to implement MPC's gas cost reduction on a volumetric basis. Because the approval is for service on and after May 2, the effect of this order will not occur until the June billing cycle.

GFG is to file compliance tariffs. Cost analysis must accompany the tariffs showing all price calculations. The Compa ny is to correct the NIP adders in its tariffs as approved and must show all calculations of the over collection that will be used to reduce the NIP account. MCC must be provided copies of all material provided the Commission.

CONCLUSIONS OF LAW

1. The Applicant, Great Falls Gas Company, furnishes gas service to consumers in Montana, and is a "public utility" under the regulatory jurisdiction of the Montana Public Service Commission. Section 69-3-101, MCA.

2. The Commission properly exercises jurisdiction over the Applicant's rates and operations. Section 69-3-102, MCA and Title 69, Chapter 3, Part 3, MCA.

3. The Commission has provided adequate public notice of all proceedings and opportunity to be heard to all interested parties in this Docket. Title 2, Chapter 4, MCA.

4. The rate level and rate structure approved herein are just, reasonable, and not unjustly discriminatory. Section 69-3-330, MCA.

ORDER

1. The Great Falls Gas Company shall file rate schedules which reflect increased annual revenues of $116,677, consistent with this Order.

2. The increased rates authorized herein shall be effective for service rendered on and after May 2, 1988.

3. Rate schedules filed shall comply with all Commission determinations set forth in this Order.

4. The Company shall file with these rate schedules its workpapers showing the calculations used to implement tariffs for this Order, per Finding No. 90.

5. The following Dockets are hereby CLOSED by this Final Order: Docket No. 86.8.38; Docket No. 86.11.62(5); Docket No. 86.12.75; Docket No. 87. 7.37

6. All motions and objections not ruled upon herein are DENIED.

DONE AND DATED this 29th day of April, 1988 by a 3-0 vote.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

CLYDE JARVIS, Chairman

TOM MONAHAN, Commissioner

DANNY OBERG, Commissioner

ATTEST:

Carol Frasier
Commission Secretary

(SEAL)

NOTE: You may be entitled to judicial review in this matter. Judicial review may be obtained by filing a petition for review within thirty (30) days of the service of this order. Section 2-4-702, MCA.